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No. 02-1809

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

J. ELLIOT HIBBS, in his official capacity as Director of the Arizona Department of Revenue,
Petitioner,

v.

KATHLEEN M. WINN, Arizona taxpayer; DIANE WOLFTHAL, Arizona taxpayer; MAURICE WOLFTHAL, Arizona taxpayer; LYNN HOFFMAN, Arizona taxpayer,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

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BRIEF OF THE COUNCIL OF STATE GOVERNMENTS, NATIONAL CONFERENCE OF STATE LEGISLATURES, NATIONAL ASSOCIATION OF COUNTIES, U.S. CONFERENCE OF MAYORS, AND INTERNATIONAL CITY/COUNTY MANAGEMENT ASSOCIATION AS *AMICI CURIAE* SUPPORTING PETITIONER

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QUESTION PRESENTED

Whether the Tax Injunction Act, 28 U.S.C. § 1341, or principles of comity, divest a federal district court of jurisdiction over a suit to enjoin a state tax credit.

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INTEREST OF THE *AMICI CURIAE*

Amici are organizations whose members include state, county, and municipal governments and officials throughout the United States.[1] *Amici* and their members have a compelling interest in legal issues that affect state and local governments.

The Court has long "recognized the important and sensitive nature of state tax systems and the need for federal-court restraint when deciding cases that affect such systems." *Fair Assessment in Real Estate Ass'n, Inc. v. McNary*, 454 U.S. 100, 102 (1981). Both "Congress and this Court repeatedly have shown an aversion to federal interference with state tax administration" as manifested by both the Tax Injunction Act, 28 U.S.C. § 1341, and the comity doctrine. *National Private Truck Council, Inc. v. Oklahoma Tax Comm'n*, 515 U.S. 582, 586 (1995).

The court of appeals nonetheless held that neither the Act nor principles of comity bar federal district court jurisdiction over a suit to enjoin a state tax credit. The court so held notwithstanding that Arizona provides an adequate remedy to challenge a tax credit in the state courts. The court's holding is contradicted by the plain text of the Act and would defeat the statute's purpose. Moreover, the comity doctrine is a further bar to this suit.

Because the court of appeals' holding poses a substantial threat to the effective administration of state tax systems,[2] *amici* submit this brief to assist the Court in its resolution of the case.

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[1] The parties have consented to the filing of this *amicus* brief and their letters of consent have been filed with the Clerk. This brief was not authored in whole or in part by counsel for a party, and no person or entity other than *amici* or their members made a monetary contribution toward its preparation or submission.

[2] This case presents no question regarding the validity of Arizona's STO credit.

SUMMARY OF ARGUMENT

1. The Tax Injunction Act (TIA) prohibits a federal district court from enjoining a state tax credit where, as here, a State provides "a plain, speedy and efficient remedy" in its courts. 28 U.S.C. § 1341. The plain text of the TIA bars a federal court from enjoining the "assessment . . . of any tax under State law." *Id.* This language is naturally understood as barring a federal court order enjoining any aspect of the scheme by which the State calculates a taxpayer's bottom line liability.

Authorities contemporaneous with the TIA's enactment establish that the term "assessment" means "determining the share of a tax to be paid by each of many persons," *Black's Law Dictionary* 151 (3d ed. 1933), or "to determine what a taxpayer shall contribute to the public." 1 *Bouvier's Law Dictionary and Concise Encyclopedia* 256 (8th ed. 1914). More recent authorities are to the same effect. *See, e.g.*, *Webster's New International Dictionary* 166 (2d ed. 1955). The process of assessment necessarily includes the reduction of a taxpayer's liability by taking credits allowed by the applicable tax code. *See* Jerome R. Hellerstein & Walter Hellerstein, *State and Local Taxation* 980 (6th ed. 1997).

The court of appeals nonetheless reasoned that Arizona's STO credit does not involve an assessment of a tax because it "is applied to the calculation of taxes *after* a taxpayer's gross income has been determined and therefore plays no part in the 'assessment' of . . . income as a basis for the imposition of taxes." Pet. App. 16a. The court's construction is contradicted by the text of the TIA, which specifically states that its jurisdictional limitation applies to "the assessment . . . of any tax," 28 U.S.C. § 1341, and not just to the assessment of income for the purpose of taxation. Indeed, under the court's reasoning, the TIA would not prohibit a federal court suit seeking to enjoin Arizona's personal exemptions and various deductions, both of which are accounted for on the State's tax

return below the determination of adjusted gross income. Moreover, a State may impose tax add-backs below the determination of taxable income. Under the court of appeals' definition of "assessment," the TIA would not prohibit a federal court suit challenging these provisions.

2. The court of appeals further reasoned that the TIA does not bar suits seeking to enjoin a tax credit because a federal court order invalidating a tax credit would not diminish the State's ability to raise revenue. Pet. App. 20a. According to the court, the Act "does not preclude federal courts from taking actions designed to increase the revenues available to the states, nor to remove unconstitutional barriers to the states' collection of the full amount of taxes they have levied or assessed." *Id.* at 23a.

Contrary to the views of the court below, this Court has recognized that the TIA has the broader purpose of "prevent[ing] federal-court interference with the assessment . . . of state taxes." *California v. Grace Brethren Church*, 457 U.S. 393, 411 (1982). Furthermore, "the legislative history of the Tax Injunction Act demonstrates that Congress worried not so much about the form of relief available in the federal courts, as about divesting the federal courts of jurisdiction to interfere with state tax administration." *Id.* at 409 n.22. The court of appeals' holding thus violates the TIA's fundamental purpose of non-interference with state tax administration even if a federal court order enjoining the STO credit would enhance Arizona's revenues.

Furthermore, the court of appeals' reasoning rests on the facile assumption that federal court orders enjoining tax credits will increase state revenues. One taxpayer's credit, however, may be another taxpayer's unconstitutional discrimination. *See, e.g., Davis v. Michigan Dept. of Treasury*, 489 U.S. 803, 805 (1989). Taxpayers might later invoke a federal judgment in state proceedings to demand refunds arguing that the constitutionality of the tax was *res judicata*.

Moreover, while it is unclear whether a federal judgment can be used to collaterally estop a state official, other taxpayers who were not parties to the federal proceeding might invoke this doctrine in state court refund suits. Thus, contrary to the holding of the court of appeals, suits challenging tax credits pose a substantial threat to state revenues.

The court's holding violates the TIA's non-interference principle for a further reason. Here, the Arizona courts have already adjudicated the validity of the STO credit and this Court has twice denied review. At best, a federal court judgment upholding the credit will needlessly waste the resources of the State in defending a statute that has already been upheld by the Arizona courts. At worst, a federal court judgment invalidating the credit will sow confusion and uncertainty by creating two conflicting judgments, neither of which has precedence over the other. It places state officials in the difficult position of risking being held in contempt by a federal court for enforcing a statute which the courts of a co-sovereign have upheld or disregarding their obligations under the state constitution to enforce state law.

3. The court of appeals further erred in reversing the district court's alternative holding that principles of comity bar federal jurisdiction over this suit. Contrary to the views of the court of appeals, *see* Pet. App. 23a-26a, the principle of federal non-interference in state tax matters is supported by an extensive line of cases and is of far broader application than acknowledged by that court.

The non-interference principle embodied in the comity doctrine is based on the recognition that the States are co-sovereigns in our federal system. This Court has catalogued the numerous reasons which underlie the non-interference principle. *See Fair Assessment*, 454 U.S. at 108 n.6 (other citation omitted).

Several of these policy concerns apply with equal force to tax credit challenges. For example, allowing tax credit challenges to be brought in federal court would subvert the States' remedial processes. Such challenges are also extraordinarily intrusive as they compel state officers to appear in federal court whenever a taxpayer challenges a credit. Furthermore, such challenges could result in conflicting judgments, subjecting state officials to incompatible legal obligations and throwing state tax administration "into disarray." *Id.* Finally, taxpayers could invoke federal judgments invalidating tax credits to assert that state officials must provide refunds. Thus, federal court jurisdiction over tax credit challenges is as potentially disruptive to state tax administration as is jurisdiction over any other taxpayer suit. Where, as here, a State provides an adequate remedy to challenge a tax credit, the comity doctrine bars a federal district court from exercising jurisdiction over the suit.

ARGUMENT

BOTH THE TAX INJUNCTION ACT AND PRINCIPLES OF COMITY BAR A FEDERAL COURT SUIT TO ENJOIN A STATE TAX CREDIT

As manifested by both the Tax Injunction Act (TIA), 28 U.S.C. § 1341, and the Court's comity jurisprudence, "Congress and this Court repeatedly have shown an aversion to federal interference with state tax administration." *National Private Truck Council, Inc. v. Oklahoma Tax Comm'n*, 515 U.S. 582, 586 (1995). The court of appeals nonetheless held that "a federal action challenging the granting of a state tax credit is not prohibited by [either] the Tax Injunction Act," Pet. App. 20a, or principles of comity. *See id.* at 23a-26a.

According to the court of appeals, "[t]he invalidation of a tax credit . . . does not adversely affect the state's ability to raise revenue," *id.* at 20a, and therefore "[t]he Tax Injunction

Act does not preclude federal courts from taking actions designed to increase the revenues available to the states, nor to remove unconstitutional barriers to the states' collection of the full amount of taxes they have levied or assessed." *Id.* at 23a. Applying the same reasoning, the court also rejected the State's assertion that the comity doctrine barred federal court jurisdiction. *See also id.* at 26a.

As explained below, the plain meaning of the Tax Injunction Act bars federal district court jurisdiction over this suit. Moreover, the court of appeals' superficial view that a federal court challenge of a state tax credit is permissible because an injunction will result in more revenues to the State is erroneous. Many federal tax challenges are based on the theory that the State is unconstitutionally favoring one class of taxpayers over another; an injunction could always be sought in federal court on the purported theory that the court's order would result in the State collecting more revenues. Affirmance of the court of appeals' holding would thus eviscerate the TIA's jurisdictional bar and the federal policy of non-interference in state tax administration. The judgment of the court of appeals should therefore be reversed.

A. Taxation Is A Core Sovereign Function

No function of government is more essential to sovereignty than the assessment and collection of taxes. *See Providence Bank v. Billings*, 29 U.S. (4 Pet.) 514, 561 (1830). "[T]axes are the lifeblood of government, and their prompt and certain availability an imperious need." *Bull v. United States*, 295 U.S. 247, 259 (1935). As the Court recognized more than 130 years ago, "[i]t is upon taxation that the several States chiefly rely to obtain the means to carry on their respective governments, and it is of the utmost importance to all of them that the modes adopted to enforce the taxes levied should be interfered with as little as possible." *Dows v. City of Chicago*, 78 U.S. (11 Wall.) 108, 110 (1871).

The Court has accordingly "long recognized that principles of federalism and comity generally counsel that courts should adopt a hands-off approach with respect to state tax administration." *National Private Truck Council*, 515 U.S. at 586. Underlying this policy in part is the practical consideration that "[t]he procedures for mass assessment and collection of state taxes and for administration and adjudication of taxpayers' disputes with tax officials are generally complex and necessarily designed to operate according to established rules." *Fair Assessment In Real Estate Ass'n, Inc. v. McNary*, 454 U.S. 100, 108 n.6 (1981) (quoting *Perez v. Ledesma*, 401 U.S. 82, 128 n.17 (1971) (Brennan, J., concurring in part and dissenting in part)).

Thus, even before the enactment of the Tax Injunction Act in 1937, this Court had repeatedly held that "[t]he scrupulous regard for the rightful independence of state governments which should at all times actuate the federal courts, and a proper reluctance to interfere by injunction with their fiscal operations, require that [federal equitable] relief should be denied in every case where the asserted federal right may be preserved without it." *Matthews v. Rodgers*, 284 U.S. 521, 525 (1932). *See also Singer Sewing Machine Co. v. Benedict*, 229 U.S. 481 (1913); *Boise Artesian Water Co. v. Boise City*, 213 U.S. 276 (1909). And even after the TIA's enactment, the Court, declining to reach the issue of whether the Act barred a federal court from granting a declaratory judgment invalidating a state tax when no injunction was sought, held that principles of comity barred the suit. *See Great Lakes Dredge & Dock Co. v. Huffman*, 319 U.S. 293, 300-01 (1943).

More recently, the Court has held that "the principle of comity" bars "§ 1983 actions against the validity of state tax systems in federal courts." *Fair Assessment*, 454 U.S. at 116. Rather, "taxpayers must seek protection of their federal rights by state remedies, provided . . . that those remedies are plain,

adequate, and complete, and may ultimately seek review of the state decisions in this Court." *Id.* at 116 (footnote omitted). "[I]n light of the strong background principle against federal interference with state taxation," the Court has further held that "§ 1983 does not call for either federal or state courts to award injunctive and declaratory relief in state tax cases when an adequate legal remedy exists." *National Private Truck Council*, 515 U.S. at 589. As these cases demonstrate, the comity doctrine's principle of non-interference with state tax administration is of broad application and is essential to the preservation of the federal-state balance.

B. The Tax Injunction Act Bars Federal District Court Jurisdiction Over Respondents' Suit

1. The Tax Injunction Act is but "one manifestation" of the "aversion to federal interference with state tax administration." *Id.* at 586. While it is only a "partial codification of the federal reluctance to interfere with state taxation," *id.* at 590, the Act "was first and foremost a vehicle to limit drastically federal district court jurisdiction to interfere with so important a local concern as the collection of taxes." *Rosewell v. LaSalle Nat'l Bank*, 450 U.S. 503, 522 (1981) (citations omitted). As the Court has further explained, "Congress' intent in enacting the Tax Injunction Act was to prevent federal-court interference with the assessment and collection of state taxes." *California v. Grace Brethren Church*, 457 U.S. 393, 411 (1982).

The Act provides that "[t]he district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State." 28 U.S.C. § 1341. As the Court has explained, "[t]he statute, on its face, yields no exception to the jurisdictional bar save where the state remedy is wanting." *Arkansas v. Farm Credit Servs. of Central Ark.*, 520 U.S. 821, 823 (1997).

The Court has further stated that "the legislative history of the [Act] demonstrates that Congress worried not so much about the form of relief available in the federal courts, as about divesting the federal courts of jurisdiction to interfere with state tax administration." *Grace Brethren Church*, 457 U.S. at 409 n.22. Recognizing both the Act's role in protecting "the federal balance" and "the basic principle that statutory language is to be enforced according to its terms," the Court has instructed that "federal courts must guard against interpretations of the Tax Injunction Act which might defeat its purpose and text." *Farm Credit*, 520 U.S. at 827.

As an initial matter, respondents cannot contend that federal court jurisdiction over their suit is needed because of Arizona's failure to provide, in the TIA's words, "a plain, speedy and efficient remedy" to challenge the STO tax credit. Indeed, shortly after the STO credit was enacted, a similar suit was fully litigated in the Arizona courts. The Arizona Supreme Court rejected this challenge in "a thoughtful and scholarly opinion on the merits of the constitutionality of the tax credit." *See* Pet. App. 7a (Kleinfeld, J., dissenting from denial of rehearing en banc) (citing *Kotterman v. Killian*, 972 P.2d 606 (Ariz. 1999)). Thereafter, this Court denied two separate petitions for a writ of certiorari. *See Kotterman, cert. denied*, 528 U.S. 921 (1999); *Rhodes v. Killian, cert. denied*, 528 U.S. 810 (1999).

The court of appeals nonetheless rejected the State's argument that federal district court jurisdiction over respondent's challenge to the STO credit is barred by the Tax Injunction Act. *See* Pet. App. 15a-23a. The court dismissed the State's contention that "the STO tax credit is part of Arizona's general system of tax 'assessment[,]'" because it "is part of the overall calculus by which the state determines how much revenue it will receive from each taxpayer." *Id.* at 16a.

Instead, the court of appeals adopted an insupportably narrow construction of the term "assessment." In the court's view, the term "has two definitions relevant to the question presented in this case: (1) 'to estimate officially the value of (property, income, etc.) as a basis for taxation,' and (2) 'to impose a tax or other charge on.'" *Id.* (quoting *Random House Dictionary of the English Language* 90 (1979)). According to the court, respondents' suit does not seek to enjoin the assessment of a state tax because "the STO credit available to a taxpayer is a uniform amount that is applied to the calculation of taxes *after* a taxpayer's gross income has been determined and therefore plays no part in the 'assessment' of . . . income as a basis for the imposition of taxes, and . . . the challenged practice is not the imposition of a tax [but] the grant of a benefit in the form of an excuse from paying a portion of the taxes already assessed." *Id.* at 16a-17a (footnote omitted).

The court further asserted that:

> Whatever a taxpayer contributes to an STO is subtracted directly from his tax bill *after* his income is assessed and his tax liability calculated. From a purely financial perspective . . . a taxpayer is unaffected by his decision as to whether or not to make an STO contribution. The funds that he may contribute will be unavailable to him in any event: they will be used either to make the contribution or to pay the taxes he owes.

Pet. App. 16a-17a n.5. The court thus concluded that a challenge to a tax credit does not "interfere with a state's '*assessment*' of a tax." *Id.* at 21a n.7. *See also id.* at 22a ("the grant of a tax credit . . . is not one of the three types of state tax procedures barred from challenge in federal court by the Tax Injunction Act").

The court of appeals found support for its construction of "assessment" by noting that one of the purposes of the TIA "was to prevent disruption of a state's efforts to collect tax

revenues." *Id.* at 18a. Asserting that it was taking a functional approach, the court broadly held "that a federal action challenging the granting of a state tax credit is not prohibited by the Tax Injunction Act. The invalidation of a tax credit, such as the one at issue here, does not adversely affect the state's ability to raise revenue[,]" but rather, "would . . . enhance[]" state coffers. *Id.* at 20a. Thus, in the event of a ruling on the merits invalidating the credit, "the Act's primary policy of non-interference with state revenue collection would not be undermined in any way." *Id.*

This sweeping holding denies the statutory language its ordinary meaning and disobeys this Court's command that "federal courts must guard against interpretations of the [Act] which might defeat its purpose and text." *Farm Credit*, 520 U.S. at 827. At a minimum, allowing tax credit challenges to be brought in federal court would eviscerate the TIA's fundamental purpose of "prevent[ing] federal court interference with the assessment . . . of state taxes." *Grace Brethren Church*, 457 U.S. at 411. Moreover, it is inaccurate to suggest -- as the court of appeals did -- that such suits will enhance state revenues. Indeed, in most cases, the opposite result is likely to occur as taxpayers who were denied the credit assert that the State engaged in unconstitutional discrimination and demand refunds by invoking the federal judgment to argue that the taxing authority is collaterally estopped from re-litigating its validity.

2. "'The starting point in statutory interpretation is the language [of the statute] itself.'" *Ardestani v. INS*, 502 U.S. 129, 135 (1991) (quoting *United States v. James*, 478 U.S. 597, 604 (1986)) (other citation and internal quotations omitted). When individual words may have multiple definitions, the Court's task is to look at the operative language in "context" and give the statute its "most natural reading." *Id.*

As relevant here, the TIA prohibits a federal court from enjoining "the assessment . . . of any tax under State law."

28 U.S.C. § 1341. Both at the time of the TIA's enactment and today, this phrase is naturally understood as prohibiting a federal court from enjoining any aspect of the scheme by which the State determines a taxpayer's bottom-line liability. As this Court noted shortly before the TIA's enactment, an assessment of income tax "include[s] the calculation and fix[es] the amount of tax payable." *Bull*, 295 U.S. at 259.

Sources contemporaneous with the TIA's enactment confirm this construction. The 1938 edition of *Webster's*, which was copyrighted in 1934, defined "assessment" as "[t]he entire plan or scheme fixed upon for charging or taxing." *Webster's New International Dictionary* 166 (2d ed. 1938). The same edition of *Webster's* defined "assess" as "[t]o determine and impose a tax." *Id.* The 1933 edition of *Black's Law Dictionary* defined the term "assessment" as "determining the share of a tax to be paid by each of many persons; or apportioning the entire tax to be levied among the different taxable persons, establishing the proportion due from each." *Black's Law Dictionary* 151 (3d ed. 1933). The same authority defined the term "assess" as "[t]o adjust or fix the proportion of a tax which each person, of several liable to it, has to pay," or "[t]o calculate the rate and amount of taxes." *Id.*

Another contemporaneous source defined "assessment" as "[d]etermining the share of a tax to be paid by each individual." *The Cyclopedic Law Dictionary* 75 (2d ed. 1922); *see also* 1 *Bouvier's Law Dictionary and Concise Encyclopedia* 256 (8th ed. 1914) (same). In defining "assessment," *Bouvier's* further stated that "[t]o assess a tax is to determine what a taxpayer shall contribute to the public." *Id. See also id.* (defining "assess" as "[t]o rate or fix the proportion which every person has to pay of any particular tax," "[t]o tax," "[t]o fix the value of," and "[t]o fix the amount of"); *see also The Cyclopedic Law Dictionary* at 75 (same).

More recent authorities likewise demonstrate that the term "assessment" means the determination of a taxpayer's bottom-line liability. Since the TIA's enactment, *Webster's* has continued to define "assessment" as "[t]he entire plan or scheme fixed upon for charging or taxing." *Webster's New International Dictionary* 166 (2d ed. 1955); *accord Webster's Third New International Dictionary* 131 (1986). Other authorities are to similar effect. *See Black's Law Dictionary* 116-17 (6th ed. 1990) ("determining the share of a tax to be paid by each of many persons . . . . [i]t fixes the liability of the taxpayer and ascertains the facts and furnishes the data for the proper preparation of the tax rolls"); *id.* (defining "assess" as "[t]o calculate the rate and amount of taxes"); *West's Tax Law Dictionary* 63 (1995) (defining "assessment" as "[t]he amount of tax, penalties, and/or interest charged to a taxpayer's account").

As the forgoing demonstrates, the assessment of a tax is the determination of the taxpayer's bottom-line liability. Put another way, it is the "Tax Due" the government, *see* Arizona Form 140 (Resident Personal Income Tax Return Line 39), whether that amount is determined by the taxing authority (as is commonly the case with property taxes) or whether it is self-assessed as is typical with income taxes. *See* Jerome R. Hellerstein & Walter Hellerstein, *State and Local Taxation* 980 (6th ed. 1997).

This process of assessment necessarily includes the reduction of a taxpayer's tax liability by taking credits allowed by the applicable tax code. As a leading authority explains, in self-assessment "[a]n individual taxpayer . . . prepares a state tax return, reporting her income and deductions, *determining her credits*, and ultimately computing her tax liability for the taxable period." *Id.* (emphasis added). Taxpayers use the same process to calculate their federal income tax liability. *See* 26 U.S.C. § 6201(a)(1) ("The Secretary shall assess all taxes determined by the taxpayer or by the Secretary as to which returns or lists are

made under this title."); *see also* IRS, Form 1040: U.S. Individual Income Tax Return (2003), at 2 (lines 44-53) (lines for inclusion of federal tax credits).[3]

These authorities conclusively refute the court of appeals' assertion that the STO credit does not involve an assessment of tax because it "is applied to the calculation of taxes *after* a taxpayer's gross income has been determined and therefore plays no part in the 'assessment' of . . . income as a basis for the imposition of taxes." Pet. App. 16a. Indeed, the court's construction is contradicted by the text of the TIA, which specifically states that its jurisdictional limitation applies to "the assessment . . . of any tax," 28 U.S.C. § 1341, and not just to the assessment of income for the purpose of taxation.

Moreover, under the court of appeals' reasoning, the TIA would not prohibit a federal court suit seeking to enjoin Arizona's personal exemptions or the various deductions allowed by state law, both of which are accounted for below the determination of adjusted gross income. *See* Arizona Form 140, at 1 (lines 16-18). Most significantly, a State may impose tax add-backs and recapture provisions below the determination of taxable income. *See id.* (line 21); New York State Dept. of Taxation and Finance, Form IT-201: Resident Income Tax Return (2002), at 2 (line 43) (requiring taxpayers to add on other state taxes); *see also* New York State Dept. of Taxation and Finance, Form IT-201-ATT: Itemized Deductions, and Other Taxes and Tax Credits (2002), at 1 (lines 17-26) (listing taxes and credits that must

[3] Under both the Federal Government's and Arizona's tax schemes, taxpayers make a preliminary calculation of tax before deducting the amount of their credits. *See* IRS Form 1040 (2003), at 2 (lines 41, 44-54, 60); Arizona Dept. of Revenue, Form 140: Resident Personal Income Tax Return (2001), at 1 (lines 19, 26-30, 39). Taxpayers do not, however, owe this amount but rather the amount determined by deducting for credits and adding back other taxes and recapture provisions. This final calculation is the amount of the assessment.

be added back). Under the court of appeals' definition of "assessment," the TIA would not prohibit a federal court suit challenging these provisions.

The court of appeals' characterization of a tax credit as "the grant of a benefit in the form of an excuse from paying a portion of the taxes already assessed," Pet. App. 17a, is contradicted by the numerous authorities above which establish that the assessment of a tax is the determination of a taxpayer's bottom-line liability. Tax credits are as integral to determining a taxpayer's liability as are the taxpayer's various sources of income, authorized exclusions from income, deductions, personal exemptions, and the applicable tax rate.[4] Indeed, nearly every State that imposes a personal income tax uses credits in their scheme. *See generally* John C. Healy & Michael S. Schadewald, *2003 Multistate Personal Income Tax Guide* 3-29—3-93 (2003). A taxpayer's failure to pay the amount of "taxes already assessed" as defined by the court of appeals, Pet. App. 17a, does not

[4] That "the STO credit available to a taxpayer is a uniform amount," Pet. App. 16a, does not make it any less a part of the process for assessing an individual taxpayer's liability. While the State has set a maximum amount of the credit, the amount that a taxpayer can take is based on a taxpayer's actual contribution to an STO. *See* Ariz. Rev. Stat. § 43-1089(A). That amount may vary from taxpayer to taxpayer. Moreover, each taxpayer's ultimate tax liability depends upon the taxpayer's income, deductions, exemptions, and credits.

Nor is it relevant in determining whether the STO credit is part of the assessment process that "[f]rom a purely financial perspective . . . a taxpayer is unaffected by his decision as to whether or not to make an STO contribution." Pet. App. 17a n.5. For those who have made STO contributions, the amount of their tax liability is affected. That the State allows taxpayers to take a credit rather than limits them to deducting their contribution in calculating their taxable income, *see id.*, does not make it any less a part of the State's scheme for assessing taxes. Nor do the TIA's text or legislative purpose support the court of appeals' distinction between deductions and credits.

subject the taxpayer to interest and penalties. Rather, a taxpayer incurs interest and penalties by failing to pay the bottom-line liability.

The court of appeals simply disregarded the ordinary meaning of the phrase "assessment . . . of any tax" in order to allow federal court challenges to state tax credits. And as explained below, the court's construction of the TIA defeats the statute's purpose.

3. Purporting to apply a "functional analysis," the court of appeals justified its construction of the TIA by reasoning that a federal court order invalidating a tax credit "does not adversely affect the state's ability to raise revenue. If the STO scheme were to be struck down on Establishment Clause grounds, Arizona's ability to raise revenue would not be diminished; to the contrary, it would be enhanced." Pet. App. 20a. Thus, "[t]he Act's primary policy of non-interference with state revenue collection would not be undermined in any way." *Id.* The court then superficially concluded that "[t]he Tax Injunction Act does not preclude federal courts from taking actions designed to increase the revenues available to the states, nor to remove unconstitutional barriers to the states' collection of the full amount of taxes they have levied or assessed." *Id.* at 23.

Contrary to the views of the court below, this Court has recognized that the TIA has the broader purpose of "prevent[ing] federal-court interference with the assessment . . . of state taxes." *Grace Brethren Church*, 457 U.S. at 411. As the Court has further stated, "the Act was first and foremost a vehicle 'to limit drastically federal district court jurisdiction to interfere with so important a local concern as the collection of taxes.'" *Farm Credit*, 520 U.S. at 826 (quoting *Grace Brethren Church*, 457 U.S. at 408-09) (other citation and quotation marks omitted).

Legislative history supports this understanding of the TIA's purpose. As this Court has explained, "the legislative history of the Tax Injunction Act demonstrates that Congress worried not so much about the form of relief available in the federal courts, as about divesting the federal courts of jurisdiction to interfere with state tax administration." *Grace Brethren Church*, 457 U.S. at 409 n.22. Contrary to the understanding of the court below, the assertion of federal district court jurisdiction in this case violates the TIA's fundamental purpose of non-interference with state tax administration even if a federal court order enjoining the credit would in this instance enhance Arizona's revenues.

In any event, the court of appeals' reasoning rests on the facile assumption that federal court orders enjoining tax credits will necessarily increase state revenues. In fact, one taxpayer's credit may be another taxpayer's unconstitutional discrimination, as evidenced by numerous cases in which tax exemptions have been challenged as discriminating against those not entitled to take them. *See, e.g., Davis v. Michigan Dept. of Treasury*, 489 U.S. 803, 806 (1989) (challenging income tax exemption for retirees of state and local governments); *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263 (1984) (challenging tax exemption for locally produced products); *Austin v. New Hampshire*, 420 U.S. 656 (1975) (challenging income tax exemption for state residents); *Dixie Tobacco & Candy Co., Inc., v. Bridges*, 246 F. Supp.2d 502 (M.D. La. 2003) (challenging tax discount for in-state wholesalers).

Contrary to the views of the court below that federal declaratory and injunctive relief invalidating tax credits would result in the State receiving greater revenues, taxpayers might later invoke a federal judgment in state proceedings to demand refunds arguing that the constitutionality of the tax was *res judicata*. Moreover, while it is unclear whether a federal judgment can be used to collaterally estop a state

official, other taxpayers who were not parties to the federal proceeding might invoke this doctrine to seek refunds in state court proceedings. *Compare Benjamin v. Coughlin*, 905 F.2d 571, 575-76 (2d Cir.) (applying non-mutual collateral estoppel to state officials), *cert. denied*, 498 U.S. 951 (1990), *with Yniguez v. Arizona*, 939 F.2d 727, 737 (9th Cir. 1991) (noting "uncertainty" whether non-mutual collateral estoppel applies to state official). *See also United States v. Mendoza*, 464 U.S. 154, 163 (1984) (holding that non-mutual offensive collateral estoppel does not apply to a suit against federal government).

The morass created by the court of appeals' rule is of particular concern for States such as Arizona. Under Arizona law, a taxpayer asserting that a tax was not "lawfully due" is not required to file a protest at the time of payment in order to later seek a refund. *See Pittsburgh & Midway Coal Mining Co. v. Arizona Dept. of Rev.*, 776 P.2d 1061, 1064 (Ariz. 1989). Rather, the protest requirement applies only when there is "a dispute between the taxpayer and the state at the time of payment." *Id.* at 1066. Moreover, under Arizona law, taxpayers have four years to file a refund claim. *See Smelkinson v. Arizona Dept. of Rev.*, No. 1814-99-TC, 2000 Ariz. Tax LEXIS 19, at *5 (Ariz. Tax Ct. 2000) (citing Ariz. Rev. Stat. § 42-1106(C)). The Arizona Supreme Court has also recently held that in a class action refund suit only the representative of the class is required to exhaust the State's administrative remedies and the filing of the representative's claim tolls the statute of limitations for all other class members. *See Arizona Dept. of Rev. v. Ladewig*, 29 P.3d 862, 869-70 (Ariz. 2001). Thus, contrary to the assertion of the court of appeals, allowing federal suits to challenge state tax credits creates a substantial threat to state revenues because of the large number of taxpayers who could file refund claims and the fact that those refund claims could cover multiple tax years.

Finally, even if there are some tax credit challenges that may not subject a State to retroactive liability, jurisdictional rules should be clear. The application of the TIA should not depend on a further inquiry by a federal court into the effect of a federal injunction on a State's finances. Indeed, such an approach not only manifestly interferes with Arizona's administration of its income tax, it also "defeat[s] [the] purpose and text" of the TIA, which divests federal district courts of jurisdiction over challenges to state taxes except for when a State's remedies are "wanting." *Farm Credit*, 520 U.S. at 823.

4. The court of appeals' holding also violates the TIA's purpose of preventing federal court interference with state tax administration by wasting state resources and inviting systemic confusion. Here, the Arizona courts have already adjudicated the validity of the STO credit and this Court has twice denied review. *See Kotterman*, 972 P.2d at 625; *cert. denied*, 528 U.S. at 921; *see also Rhodes*, 528 U.S. at 810.

At best, a federal court judgment upholding the credit will needlessly waste the resources of the State in defending a statute that has already been upheld by the Arizona courts. Such duplicative litigation will also consume the time of the federal courts, as this case illustrates. *See* Pet. App. 27a-36a (district court order dismissing case for lack of subject matter jurisdiction).

At worst, a federal court judgment invalidating the credit will sow confusion and uncertainty by creating two conflicting judgments, neither of which has precedence over the other. It places state officials in the difficult position of risking being held in contempt by a federal court for enforcing a statute which the courts of a co-sovereign have upheld or disregarding their obligations under the state constitution to enforce state law.

Ultimately, and after years of litigation, this Court will be required to resolve the conflict. The exercise of federal district court jurisdiction in this case would thus not only directly conflict with the TIA's non-interference principle as a doctrinal matter, it would also lead to the confusion and uncertainty that the Act is intended to prevent. *See Grace Brethren Church*, 457 U.S. at 409 n.22, 411.

C. The Comity Doctrine Bars Federal District Court Jurisdiction Over This Suit

The court of appeals further erred in reversing the district court's alternative holding that this Court's comity jurisprudence precludes federal jurisdiction over respondents' suit. The court supported its ruling on this point by mischaracterizing the district court's holding as a "broad bar to the litigation of federal constitutional claims in federal court [which] is unsupported by precedent." Pet. App. 23a.

According to the court of appeals, this Court "has twice held federal jurisdiction to be barred by the doctrine of comity" in state tax challenges. *Id.* at 23a; *see also id.* at 23a-25a (citing *Fair Assessment*, 454 U.S. at 115, & *Great Lakes Dredge*, 319 U.S. at 297). The court explained that these were "cases in which the plaintiffs sought to stop the collection of a tax; thus, they are fundamentally different from the instant case." *Id.* Repeating its dubious premise that invalidation of the STO credit would enhance state revenues, *see* discussion *supra* 17-19, the court further reasoned that "Arizona identifies no harm that renders federal court review of this statute any more intrusive on the state's sovereignty than the review of any other state statute that is alleged to be unconstitutional." Pet. App. 26a. The court thus concluded that the comity doctrine "does not bar plaintiffs' attempt to vindicate the important constitutional rights at issue" and reversed the district court's order dismissing the case. *Id.*

The court of appeals' holding manifests a superficial and incomplete understanding of the history and scope of the comity doctrine in state tax matters. Contrary to the understanding of the court, the principle of federal non-interference in state tax matters is supported by a far more extensive line of cases than the two cited by the court. Indeed, the principle can be traced back at least as far as *Dows v. City of Chicago*, 78 U.S. (11 Wall.) 108, 110 (1871), and is supported by numerous cases. *See* discussion *supra* at pp. 5-8. It is also of far broader application than acknowledged by the court below. *See, e.g., National Private Truck Council*, 515 U.S. at 589 (holding "in light of the strong background principle against federal interference with state taxation" that "§ 1983 does not call for either federal or state courts to award injunctive or declaratory relief in state tax cases when an adequate legal remedy exists"); *McKesson Corp. v. Division of Alcoholic Beverages & Tobacco*, 496 U.S. 18, 51 (1990) (noting that the States are afforded great flexibility in satisfying the requirements of due process in the field of taxation); *First Nat'l Bank v. Board of Comm'rs*, 264 U.S. 450, 454-56 (1924) (holding that failure to exhaust state administrative remedy bars refund suit in federal court).

The non-interference principle embodied in the comity doctrine is based on the recognition that the States are co-sovereigns in our federal system. *See, e.g., Fair Assessment*, 454 U.S. at 108 (quoting *Matthews v. Rodgers*, 284 U.S. at 525) ("'The scrupulous regard for the rightful independence of state governments which should at all time actuate the federal courts, and a proper reluctance to interfere by injunction with their fiscal operations, require that [injunctive] relief should be denied in every case where the asserted

federal right may be preserved without it.'"). In *Fair Assessment*, the Court catalogued the numerous reasons which underlie the non-interference principle:

> The special reasons justifying the policy of federal noninterference with state tax collection are obvious. The procedures for mass assessment and collection of state taxes and for administration and adjudication of taxpayers' disputes with tax officials are generally complex and necessarily designed to operate according to established rules. State tax agencies are organized to discharge their responsibilities in accordance with the state procedures. If federal declaratory relief were available to test state tax assessments, state tax administration might be thrown into disarray, and taxpayers might escape the ordinary procedural requirements imposed by state law. During the pendency of the federal suit the collection of revenue under the challenged law might be obstructed, with consequent damage to the State's budget, and perhaps a shift to the State of the risk of taxpayer insolvency. Moreover, federal constitutional issues are likely to turn on questions of state tax law, which, like issues of state regulatory law, are more properly heard in the state courts.

454 U.S. at 108 n.6 (quoting *Perez v. Ledesma*, 401 U.S. 82, 128 n.17 (1971) (Brennan, J., concurring in part and dissenting in part)).

Several of these policy concerns apply with equal force to tax credit challenges. As a general matter, allowing tax credits challenges to be brought in federal court would subvert the State's remedial processes. Furthermore, as explained at pp. 17-20, *supra*, such challenges are extraordinarily intrusive as they "would hale state officers into federal court every time" a taxpayer challenged a tax credit. *Id.* at 115. Moreover, such challenges could result in conflicting judgments and subject state officials to incompatible

legal obligations and thus throw state tax administration "into disarray." *Id.* at 108 n.6. Indeed, respondents' purpose in bringing this litigation in federal court is to obtain a judgment that conflicts with the Arizona Supreme Court's decision upholding the credit. *See Kotterman*, 972 P.2d at 616. Finally, as explained above, in many instances taxpayers could invoke federal judgments invalidating tax credits to assert that state officials must provide refunds. Federal court jurisdiction over tax credit challenges is thus as "potentially disruptive" to state tax administration as is jurisdiction over any other taxpayer suit. *National Private Truck Council*, 515 U.S. at 591.

Nor can it be forgotten that in the *Kotterman* suit, the Arizona courts provided a full and fair hearing on the same federal claim raised by respondents. The judges of the Arizona courts "take the same oath to uphold the federal Constitution that [federal judges] do." Pet. App. 8a (Kleinfeld, J., dissenting from denial of rehearing en banc). Indeed, "[t]he Arizona Supreme Court provided a thoughtful and scholarly opinion on the merits of the constitutionality of the [STO] credit," *id.* at 7a, which this Court twice declined to review. That a panel of a federal court of appeals may not agree with the Arizona Supreme Court's judgment is a patently insufficient basis to disregard the non-interference principle, which is the essence of the comity doctrine.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted,

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